GRAND TOYS INTERNATIONAL INC
Form 10-Q/A
July 02, 2004

FORM 10-Q/A-2

Securities and Exchange Commission

Washington, D.C. 20549

(Mark One)

[**X**]

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended: **March 31, 2004**

[ ]

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the transition period from _______________ to _______________.

Commission File No. 0-22372.

GRAND TOYS INTERNATIONAL, INC.

(Exact Name of Registrant as Specified in its Charter)

Nevada

98-0163743

(State or other jurisdiction of

(I.R.S. Employer

incorporation or organization

Identification No.)

1710 Route Transcanadienne, Dorval, Quebec, Canada, H9P 1H7

(Address of principal executive offices)

(514) 685-2180

(Registrant s telephone number, including Area Code)

(Former name, former address and former fiscal year,

if changed since last report)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes

X

No _____

Indicate the number of shares outstanding of each of the Issuer s classes of common equity, as of May 14, 2004: 5,355,244

This is Amendment No. 2 to the Grand Toys International, Inc. Quarterly Report on Form 10-Q for the period ended March 31, 2004, as originally filed on May 14, 2004. No changes have been made to the Company's balance sheet or cash flow statements as they appeared in our May 14, 2004 Form 10-Q. A change was made to the Company's consolidated statements of operations removing shipping and handling costs charged to customers and cooperative advertising from general and administrative expenses and presenting them as part of net sales. Changes were also made to management's discussion and analysis and results of operations to conform to the changes made to the net sales and general and administrative expenses.

The company has not updated the Form 10-Q to modify disclosures in the Form 10-Q for events occurring subsequent to the original May 14, 2004 filing date. This Amendment No. 2 to Form 10-Q continues to speak as of May 14, 2004.

GRAND TOYS INTERNATIONAL, INC.

Index to Quarterly Report on Form 10 Q/A-2
Filed with the Securities and Exchange Commission
Period ended March 31, 2004

GRAND TOYS INTERNATIONAL, INC.

Part I. Financial Information

Item 1. Consolidated Financial Statements

Consolidated Balance Sheets

	March 31, 2004 (Unaudited)	December 31, 2003
Assets		
Current assets:		
Cash	$ 1,064,628	$ 1,487,318
Short-term deposit (note 14(c))	500,000	500,000
Accounts receivable (net of allowance for doubtful accounts of $9,603; 2003 - $9,712)	1,984,671	1,598,907
Due from Playwell International Limited	1,052,897	804,252
Due from employees	3,127	771
Current portion of loan receivable (note 2)	163,881	161,447
Inventory	1,726,062	1,682,298
Prepaid expenses (note 3)	456,909	367,288
Total current assets	6,952,175	6,602,281
Note receivable (note 9)	183,528	286,896
Loan receivable (note 2)	179,069	220,963
Equipment and leasehold improvements, net (note 4)	211,348	219,988
Other assets (note 5)	11,003	13,331
Total assets	$ 7,537,123	$ 7,343,459

GRAND TOYS INTERNATIONAL, INC.

Consolidated Balance Sheets

		March 31, 2004 (Unaudited)		December 31, 2003
Liabilities and Stockholders' Equity				
Current liabilities:				
Bank indebtedness (note 6)	$	1,800,050	$	1,579,458
Trade accounts payable		978,945		1,047,390
Other accounts payable and accrued liabilities		207,499		217,567
Accrued compensation		59,417		111,085
Accrued legal expenses		55,163		151,711
Total current liabilities		3,101,074		3,107,211
Minority interest		100		100
Stockholders' equity:				
Capital stock (note 7):				
Voting common stock, $0.001 par value:				
12,500,000 shares authorized,				
5,355,244 shares issued and outstanding		5,355		5,355
Additional paid-in capital		22,750,942		22,750,518
Deficit		(17,731,951)		(17,968,179)
Accumulated other comprehensive income-cumulative currency translation adjustment		(588,397)		(551,546)
		4,435,949		4,236,148
Commitments and contingencies (notes 13 and 14)				
Total liabilities and stockholders' equity	$	7,537,123	$	7,343,459

See accompanying notes to unaudited consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Consolidated Statements of Operations (Unaudited)

	For the three months ended March 31,	
	2004	2003
Net sales	$ 2,813,698	$ 2,907,332
Cost of goods sold	1,674,605	1,689,518
Gross profit	1,139,093	1,217,814
Operating costs and expenses:		
General and administrative	499,421	529,093
Salaries and fringe benefits	337,889	294,702
Royalties	22,874	69,895
Bad debt expense	12,939	10,601
Depreciation and amortization	13,427	16,419
	886,550	920,710
Non-operating expense (income)		
Interest expense	19,446	20,737
Interest revenue	(14,130)	(14,894)
Foreign exchange loss (gain)	10,999	(59,144)
	16,315	(53,301)
Earnings before income taxes	236,228	350,405
Income tax expense	-	325
Earnings from continuing operations	236,228	350,080
Gain on sale of discontinued operations	-	103,002
Net earnings applicable to common stockholders	$ 236,228	$ 453,082
Earnings per share (note 10):		

Continuing operations:				
Basic	$	0.04	$	0.13
Diluted		0.04		0.06
Discontinued operations:				
Basic		-		0.03
Diluted		-		0.02
Net earnings:				
Basic		0.04		0.16
Diluted	$	0.04	$	0.08

See accompanying notes to unaudited consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Consolidated Statements of Stockholders' Equity and Comprehensive Income (Unaudited)

	Capital Stock	Additional Paid in Capital	Deficit	Accumulated other comprehensive income	Total
January 1, 2004	$ 5,355	$ 22,750,518	$ (17,968,179)	$ (551,546)	$ 4,236,148
Net earnings for the period	-	-	236,228	-	236,228
Foreign currency adjustment	-	-	-	(36,851)	(36,851)
Total comprehensive income					199,377
Compensation expense	-	424	-	-	424
March 31, 2004	$ 5,355	$ 22,750,942	$ (17,731,951)	$ (588,397)	$ 4,435,949

See accompanying notes to unaudited consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Consolidated Statements of Cash Flows (Unaudited)

	For the three months ended March 31, 2004	2003
Cash flows from operating activities:		
Net earnings from continuing operations	$ 236,228	$ 350,080
Adjustments for:		
Depreciation and amortization	13,427	16,419
Amortization of product development costs	2,164	763
Compensation expense	424	930
Net change in non-cash operating working capital items (note 11)	(1,020,674)	(687,118)
Net cash used for operating activities from continuing operations	(768,431)	(318,926)
Cash flows from financing activities:		
Increase (decrease) in bank indebtedness	211,977	(9,914)
Decrease in loan payable to a director	-	(14,570)
Increase (decrease) in due from employees	(2,348)	442
Other	(1,618)	(2,318)
Net cash provided by (used for) financing activities	208,011	(26,360)
Cash flows from investing activities:		
Loan receivable	39,460	51,409
Proceeds from note receivable	103,368	178,239
Decrease in other assets	2,163	9,056
Additions to equipment and leasehold improvements	(7,261)	(530)
Net cash provided by investing activities	137,730	238,174
Net decrease in cash and cash equivalents	(422,690)	(107,112)
Cash and cash equivalents, beginning of period	1,487,318	540,896
Cash and cash equivalents, end of period	$ 1,064,628	$ 433,784

Supplemental disclosure of cash flow information (note 12)

See accompanying notes to unaudited consolidated financial statements.

GRAND TOYS INTERNATIONAL, INC.

Notes to Unaudited Consolidated Financial Statements

Grand Toys International, Inc. (the Company), a Nasdaq SmallCap listed Company, is organized under the laws of the State of Nevada. Its principal business activity, through its wholly-owned Canadian and US operating subsidiaries, is the distribution of toys and related items.

1.

Significant accounting policies:

(a)

Principles of consolidation:

These consolidated financial statements, presented in US dollars and in accordance with accounting principles generally accepted in the United States, include the accounts of the Company and its subsidiaries. All significant intercompany balances and transactions have been eliminated.

(b)

Revenue recognition:

Sales are recognized at the time of shipment of products. The Company estimates liabilities and records provisions for customer allowances as a reduction of revenue, when such revenue is recognized.

Net sales include gross revenues, freight charged to clients and FOB commissions, net of allowances and discounts such as defectives, returns, volume rebates, cooperative advertising, cash discounts, customer fines, new store allowance, markdowns, freight and warehouse allowance.

(c)

Cost of Goods Sold:

Cost of Sales include cost of merchandise, duties, brokerage fees, inbound freight, packaging, product development and provision on slow-moving inventory.

(d)

General and Administrative Costs:

General and Administrative costs include advertising expense, royalties, rent, insurance costs, travel and entertainment, utilities, courier, repairs and maintenance, communications expense, office supplies, professional fees, dues and membership, bank charges and property taxes expense.

Outbound shipping and handling costs incurred by the Company are included in general and administrative expense. For the period ended March 31, 2004, freight out was $16,567.

(e)

Inventory:

Inventory is valued at the lower of cost, determined by the first in, first out method, and net realizable value. The only significant class of inventory is finished goods.

(f)

Prepaid expenses:

Prepaid expenses primarily include insurance, advances on inventory purchases, current portion of royalties and real estate taxes. Insurance costs are written off over the term of the respective policies.

Prepaid royalties relate to licensing agreements for character properties. These contracts can extend for up to three years. Total expense for the three-month period ended March 31, 2004 was $22,874 (2003 - $69,895) and is shown as royalty expense in the statements of operations.

Prepaid taxes are amortized on a straight-line basis over the period to which they relate. The amount expected to be recognized in the statement of operations in 2004 is $86,937.

(g)

Other assets:

Prepaid royalties are capitalized and amortized as earned in relation to product sales, over a period not to exceed the term of the related agreements. The amounts expected to be recognized in the statement of operations during the remainder of 2004 and the year 2005 are $1,610 and $12,700, respectively.

Product development costs for proprietary product lines are capitalized and written off over a period of twenty-four months, the estimated life of a new product. If a product is abandoned the related costs are written off immediately.

GRAND TOYS INTERNATIONAL, INC.

Notes to Unaudited Consolidated Financial Statement

1.

Significant accounting policies (continued):

(h)

Equipment and leasehold improvements:

Equipment and leasehold improvements are stated at cost less accumulated depreciation.

Depreciation methods and annual rates adopted by the Company are as follows:

Asset	Method	Rate/period
Computer equipment	Declining balance	30%
Machinery and equipment	Declining balance	20%
Furniture and fixtures	Declining balance	20%
Trucks and automobiles	Declining balance	30%
Telephone equipment	Declining balance	30%
Leasehold improvements	Straight-line	Term of lease plus one renewal term

(i)

Incomes taxes:

The Company follows the asset and liability method of accounting for income taxes. Under the asset and liability method, the change in the net deferred tax asset or liability is included in the computation of net income. Deferred tax assets and liabilities are measured using enacted or substantively tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. Deferred tax assets are evaluated and, if realization is not considered to be more likely than not , a valuation allowance is provided.

(j)

Foreign currency translation:

i)

Grand Toys Ltd., a wholly-owned Canadian subsidiary, uses the Canadian dollar as its functional currency. Financial statements of the self-sustaining foreign operation are translated into US dollars using the exchange rate prevailing at the balance sheet date for assets and liabilities and the average exchange rate for the year for revenues, expenses and cash flows. The resulting currency translation adjustments are accumulated and reported in other comprehensive income.

ii)

Other monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate prevailing at the balance sheet date. Revenues and expenses denominated in foreign currencies are translated at the rate of exchange prevailing at the transaction dates. All exchange gains and losses are included in income.

(k)

Guarantees:

In November 2002, the Financial Accounting Standards Board (FASB) Interpretation No.45, *Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness to Others*, was issued. This Interpretation enhances the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under guarantees issued. The Interpretation also clarifies that a guarantor is required to recognize, at inception of a guarantee, a liability for the fair value of the obligation undertaken. The initial recognition and measurement provisions of the Interpretation were applicable to guarantees issued or modified after December 31, 2002 and the disclosure requirements were effective for financial statements of interim or annual periods ending after December 15, 2002. The Company was not a party to any guarantees as at March 31, 2004 and March 31, 2003.

(l)

Earnings per Share:

i)

Basic earnings per share are determined by dividing the weighted average number of common shares outstanding during the period into net earnings.

ii)

Diluted earnings per share give effect to all potentially dilutive common shares that existed at March 31, 2004.

(m)

Advertising and Promotion:

All costs associated with advertising and promoting products are included in the statement of operations in the period incurred. Media advertising expense for the period ended ended March 31, 2004 and 2003 were $15,792 and $56,978 respectively and are shown as part of general and administrative expenses in the financial statements. Cooperative advertising expense for the period ended ended March 31, 2004 and 2003 were $41,942 and $46,696 respectively and are shown as a reduction of revenues in the financial statements.

Slotting fees are recorded as a deduction of gross sales. These fees are determined annually on a customer by customer basis.

(n)

Employee stock option plan:

The Company accounts for its employee stock option plan in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*. As such, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeds the exercise price. Financial Accounting Standards Board ("FASB") Statement No. 123, *Accounting for Stock-Based Compensation*, allows entities to continue to apply the provisions of APB Opinion No. 25 and requires pro-forma net earnings and pro-forma earnings per share disclosures for employee stock option grants as if the fair-value-based method defined in FASB Statement No. 123 had been applied. This disclosure is included in the notes to these financial statements.

(o)

Comprehensive income:

Comprehensive income consists of net income and cumulative currency translation adjustments and is presented in the consolidated statements of stockholders equity and comprehensive income.

(p)

Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(q)

Cash and cash equivalents:

The Company considers all liquid investments with maturities of three months or less when acquired to be cash equivalents.

2.

Loan receivable:

The loan receivable is due from Limited Treasures Inc. ("Limited Treasures"). The loan is secured by accounts receivable and inventory and personal guarantees of the stockholders of Limited Treasures.

In June 2001, the Company settled a litigation it had commenced against Limited Treasures. Under the terms of the Settlement Agreement, Limited Treasures agreed to pay $775,000 over 48 months commencing June 2001 and ending May 2005. Interest, which was charged at the rate of 9.0% per annum under the original loan, was revised to 6.0% per annum in April 2003, reducing the monthly payment.

Details are as follows:

	March 31, 2004	December 31, 2003

Amount due repayable in monthly payments of principal and interest of $7,500 until November 30, 2001, $21,124 until March 31, 2003 and $15,000 until April 2005, with a final payment of $165,789 in May 2005	$	342,950	$	382,410
Less current portion		163,881		161,447
	$	179,069	$	220,963

3.

Prepaid expenses:

		March 31, 2004		December 31, 2003
Prepaid inventory	$	178,749	$	66,555
Royalties		14,310		14,821
Insurance		90,359		192,699
Other		173,491		93,213
	$	456,909	$	367,288

4.

Equipment and leasehold improvements:

	March 31, 2004			December 31, 2003		
	Cost		Accumulated depreciation	Cost		Accumulated depreciation
Computer equipment	$ 1,477,393	$	1,337,965	$ 1,486,846	$	1,342,114
Machinery and equipment	506,320		494,379	512,100		499,387
Furniture and fixtures	551,188		531,857	557,376		536,840
Trucks and automobiles	93,192		92,781	94,256		93,806
Telephone equipment	51,499		45,687	52,086		45,900
Leasehold improvements	287,662		253,237	290,945		255,574
	$ 2,967,254	$	2,755,906	$ 2,993,609	$	2,773,621
Net book value		$	211,348		$	219,988

5.

Other assets:

		March 31, 2004		December 31,2003
Prepaid royalties	$	14,310	$	14,821
Product development costs		11,003		13,331
		25,313		28,152
Less current portion of prepaid royalties, included in prepaid expenses		14,310		14,821
	$	11,003	$	13,331

6.

Bank indebtedness:

The Company has a line of credit to finance its inventory and accounts receivable for advances of up to $2,669,000 (CA$3,500,000). The receivable loan has a discount fee of 2.0% and the inventory loan bears interest at Canadian prime plus 7.5%. The agreement is for a period of one year and is renewed automatically, unless prior notice is given by either party.

The loan is secured by a first lien in the principal amount of $3,050,000 (CA$4,000,000) on the universality of all present and future assets of the Company and the assignment of insurance. There are no debt covenants or cross-default provisions.

As at March 31, 2004, the Company had approximately $869,000 (December 2003 - $1,120,000) of credit available under this facility, subject to the availability of eligible inventory and accounts receivable.

7.

Capital stock

(a)

Authorized capital also includes 5,000,000, $0.001 par value preferred shares, issuable in series with such designation, rights and preferences as may be determined from time to time by the Board of Directors. There are no preferred shares issued and outstanding at March 31, 2004.

(b)

Share transactions:

i)

April 2003:

The 10,144 common shares issued in October 2002 were repurchased for a total consideration of $12,982, decreasing capital stock by $10. The shares were subsequently cancelled.

ii)

August 2003:

82,609 common shares were issued in settlement of consulting fees, increasing capital stock by $82.

iii)

November 2003:

2,520,000 warrants were exercised for total consideration of $25,200, increasing capital stock by $2,520.

(c)

The number of shares of common stock outstanding is as follows:

There were no transactions in the period presented.

	March 31, 2004	December 31, 2003
Common Stock	5,355,244	5,355,244

8.

Stock options and warrants:

The Company's amended and restated employee stock option plan (the "Option Plan") provides for the issuance of up to 300,000 options to acquire common shares of the Company. Stock options granted under the Option Plan may be Incentive Stock Options under the requirements of the Internal Revenue Code, or may be Non-statutory Stock Options which do not meet such requirements. Options may be granted under the Option Plan to, in the case of Incentive Stock Options, all employees (including officers) of the Company, or, in the case of Non-statutory Stock Options, all employees (including officers) or non-employee directors of the Company.

Under the Option Plan, the exercise price of each option granted has been equal to the market price of the Company s stock on the grant date and an option s maximum term is ten years.

Changes in options and warrants are as follows:

	Option Plan	Other stock options	Warrants	Total		Weighted-average exercise price per share
January 1, 2004	213,464	196,000	637,143	1,046,607	$	1.74
Granted	875	-	-	875		3.02
Options outstanding and exercisable at March 31, 2004	214,339	196,000	637,143	1,047,482	$	1.74

The following table summarizes information about options and warrants outstanding and exercisable at March 31, 2004:

		Options and warrants outstanding and exercisable		
Range of exercise prices	Number		Weighted-average exercise price	Weighted-average remaining contractual life (yrs)
$0.01 - $1.96	554,214	$	0.59	7.69
$2.12 - $3.07	476,768		2.20	2.09
$5.62 - $11.00	1,000		7.78	6.32
$16.00 - $87.60	15,500		28.13	4.11
	1,047,482	$	1.74	5.09

Pro-forma information regarding net earnings and earnings per share is required by FASB Statement No. 123, and has been determined as if the Company had accounted for its employee stock options under the fair value method of that statement.

The Company s pro-forma net earnings and earnings per share are as follows:

		March 31, 2004		March 31, 2003
Earnings from continuing operations, as reported	$	236,228	$	350,080
Add compensation cost resulting from:				
Application of variable accounting to modified awards (APB Opinion No. 25)		424		930
Application of fair value method (FASB Statement No. 123)		(1,873)		(1,418)
Pro-forma earnings from continuing operations		234,779		349,592
Earnings from discontinued operations		-		103,002
Pro-forma net earnings applicable to common stockholders	$	234,779	$	452,594
<u>Basic EPS</u>				
Earnings from continuing operations	$	0.04	$	0.13
Earnings from discontinued operations		-		0.03
Net earnings applicable to common stockholders	$	0.04	$	0.16
<u>Diluted EPS</u>				
Earnings from continuing operations	$	0.04	$	0.06
Earnings from discontinued operations		-		0.02
Net earnings applicable to common stockholders	$	0.04	$	0.08

The pro-forma amounts include compensation cost as calculated using the Black-Scholes option pricing model with the following assumptions:

	March 31, 2004	March 31, 2003
Weighted average expected life (years)	3.0	3.0
Risk-free interest rate	2.10%	1.98%

Volatility factor of expected market price of Company s common stock		119%		142%
Dividend rate		-		-
		March 31, 2004		March 31, 2003
Weighted average grant date fair value of options and warrants	$	2.14	$	1.47

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company s stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect their fair value estimate, in management s opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its stock options.

Compensation expense of $424 and $930 was recorded for the three-month periods ended March 31, 2004 and 2003, respectively, as a result of the application of variable accounting to modified awards.

9.

Discontinued operations:

On June 14, 2002, the Company sold its investment in its wholly-owned subsidiary, Sababa Toys Inc. ("Sababa"), to the subsidiary's management for $1,065,716. Consideration received by the Company was a promissory note secured by the shares of Sababa. The assets and liabilities of Sababa, together with the sales and expenses for the period to June 14, 2002 and the comparative figures for the year ended December 31, 2001, have been classified as discontinued operations.

The promissory note is being repaid using cash collected on accounts receivable and inventories, net of liabilities existing as at June 14, 2002, and 10% of net sales of inventories acquired after that date. Any balance owing will be due on June 30, 2005.

The Company calculated the cost of its investment in Sababa using the equity method and recorded a gain on the sale of $761,584 of which $497,800 was deferred as at December 31, 2002. In 2003, the conditions which existed at the date of sale which required the initial deferral of the gain were removed. As a result, the company recognized the balance of the gain in the statement of operations during the year.

The table below summarizes the periods in which the gain was recorded and cash applied against the note receivable:

		Deferred Gain		Note receivable
Balance, January 01, 2003	$	497,800	$	884,877
Recorded in 2003		(497,800)		(597,981)

Balance, December 31, 2003		-		286,896
Recorded in 2004		-		103,368
Balance, March 31, 2004	$	-	$	183,528

10.

Earnings per share:

		Income (numerator)	Shares (denominator)		Per Share Amount
Quarter ended March 31, 2004					
Basic EPS					
Earnings from continuing operations	$	$236,228	5,355,244	$	0.04
Earnings applicable to common stockholders and assumed conversions		236,228	5,355,244		0.04
Diluted EPS					
Earnings from continuing operations	$	236,228	5,964,818	$	0.04
Earnings applicable to common stockholders and assumed conversions		236,228	5,964,818		0.04

		Income (numerator)	Shares (denominator)		Per Share Amount
Quarter ended March 31, 2003					
Basic EPS					
Earnings from continuing operations	$	350,080	2,762,698	$	0.13
Earnings from discontinued operations		103,002	2,762,698		0.03
Earnings applicable to common stockholders and assumed conversions		453,082	2,762,698		0.16
Diluted EPS					
Earnings from continuing operations	$	350,080	5,602,889	$	0.06
Earnings from discontinued operations		103,002	5,602,889		0.02

Earnings applicable to common stockholders and assumed conversions	453,082	5,602,889	0.08

As of March 31, 2004, options and warrants to purchase 16,500 shares (March 2003 378,768) of the Company s common stock were not included in the diluted earnings per share calculation as their effect is anti-dilutive.

GRAND TOYS INTERNATIONAL, INC.

Notes to Unaudited Consolidated Financial Statements

11.

Net change in non-cash operating working capital items:

		For the three months ended March 31, 2004		2003
Continuing operations:				
Increase in accounts receivable	$	(402,492)	$	(22,688)
Increase in amount due from Playwell International Limited		(248,645)		-
Increase in inventory		(62,350)		(525,930)
Increase in prepaid expenses		(93,842)		(14,964)
Decrease in trade accounts payable		(58,739)		(216,672)
(Decrease) increase in other accounts payable and accrued liabilities		(8,067)		87,889
Decrease in accrued compensation		(50,081)		(17,978)
(Decrease) increase in accrued legal expenses		(96,458)		23,225
	$	(1,020,674)	$	(687,118)

12.

Supplemental disclosure of cash flow information:

		For the three months ended March 31 2004		2003
Supplemental disclosure of cash flow information:				
Cash paid during the period for:				
Interest	$	19,446	$	20,737
Income taxes		-		325

13.

Commitments:

The Company has entered into long-term leases with minimum annual rental payments for the next five years and thereafter approximately as follows:

2004	252,000
2005	349,000
2006	349,000
2007	344,000
2008	340,000
Thereafter	244,000

Rent expense for the period ended March 31, 2004, and 2003 amounted to approximately $36,218 and $32,788, respectively.

The Company has entered into a long-term agreement to sub-lease a portion of its warehouse, resulting in a reduction of the minimum annual rental payments presented above of approximately $135,000 for the remainder of 2004 and $182,000 annually from 2005 to 2007.

14.

Contingencies:

(a)

A lawsuit for alleged breach of contract has been filed against the Canadian subsidiary by a former sales representative. In the opinion of management, this action has no merit. At this point in time, it is difficult to ascertain or estimate the value of a settlement, if any.

(b)

On May 21, 2003, the Company was named in a lawsuit for alleged defective product causing personal injury and was acting as an agent for the vendor. A defense has been filed denying liability and the claim is covered by insurance. At this point in time, it is difficult to ascertain an estimate of the value of a settlement, if any.

(c)

The Company s Canadian subsidiary is contingently liable for an outstanding letter of credit of $500,000 as at March 31, 2004. The short-term deposit has been pledged as collateral for this letter of credit.

(d)

On April 15, 2004, The Company was named in a lawsuit for alleged non payment of commissions. In the opinion of management, it is difficult to ascertain or estimate the value of a settlement if any.

15.

Segment information:

(a)

Operating and geographic information:

The Company operates primarily in one segment which includes the distribution of toys and related items. Nearly all sales are to Canadian customers. The majority of long-lived assets are located in Canada.

(b)

Other information:

		March 31, 2004			March 31, 2003	
		Revenue	%		Revenue	%
Customer A	$	703,424	25	$	726,833	25

B	619,014	22	581,466	20
C	281,370	10	203,513	